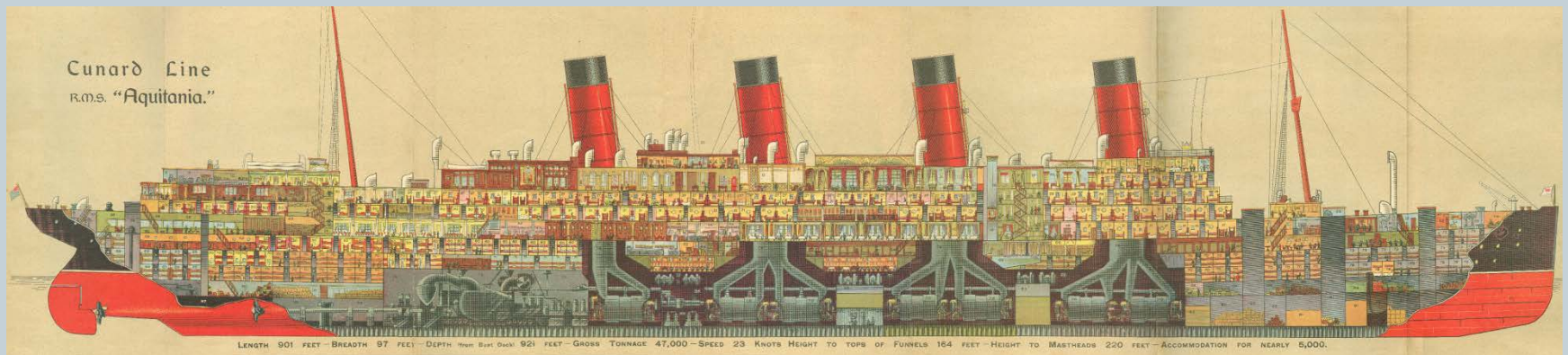


# FOREST OIL (FST)



## CHRISTOPHER KARLIN AQUITANIA CAPITAL MANAGEMENT, LLC



VALUEx VAIL

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# Who We Are



- Aquitania Capital Management is an opportunistic value investor with an event focus
- Seeking dislocations where our counterparties are making uneconomic decisions
  - Asymmetric reward-to-risk situations with high conviction in a variant thesis
  - Securities that are either being accidentally overlooked or actively avoided by most investors

# Opportunity



- Forest Oil and Sabine Oil & Gas agreed to merge on 5/6/14
- Merger creates value for both parties
- Market fails to recognize value for identifiable structural reasons
- FST trades at a substantial discount to intrinsic value
- Margin of safety highlights gap between perceived risk and probable risk
- Several near-term catalysts to close valuation gap with peers
- Long-term catalysts could result in substantial growth
- Primary risks are deal closure and energy pricing – primarily natural gas

# Merger Rationale



- Sabine:

- Public listing – liquidity and capital access
- Additional scale – reserves & production
- Acquires reserves at a discount
- Sabine management remains in place

- Forest:

- Improves balance sheet
- Participates in upside

- 2015 synergies:

- Eliminate 2/3 of Forest SG&A
- Apply Sabine's D&C talent and Forest's cost control to improve returns on Forest reserves.

# Forest Oil



- Forest Oil is an asset-rich domestic E&P company with a weak balance sheet
- Stock has significantly underperformed:
  - 2011: -50%
  - 2012: -53%
  - 2013: -46%
  - 2014 YTD (pre-merger announcement): -50%
  - 2014 YTD (6/17/14): -36%
- Assets: Ark-La-Tex (gas), Eagle Ford (oil) & Permian (oil)
- High indebtedness, large drilling program and weak drilling results pushed it to seek a partner

# Sabine Oil & Gas



- Founded in 2007 by First Reserve (energy PE firm) and team from Devon
- Focused on East Texas (gas), Eagle Ford (oil) and Granite Wash (oil)
- Have demonstrated very effective drilling and completion results
- Strong Production Growth 38% CAGR 2008 – 2014E
- Wanted a public listing for capital access and PE liquidity

# Why Is FST Mispriced?



- Size

- FST is a \$2.30 stock with a \$274MM market cap – limited institutional interest

- ✦ Implicit combined market cap is  $\$274\text{MM}/0.265 = \$1.0\text{B}$

- Complexity

- Sabine is private – need to value Sabine off fundamentals to value deal

- Disgust

- FST has chronically disappointed. Who is still watching?



# Deal Mechanics

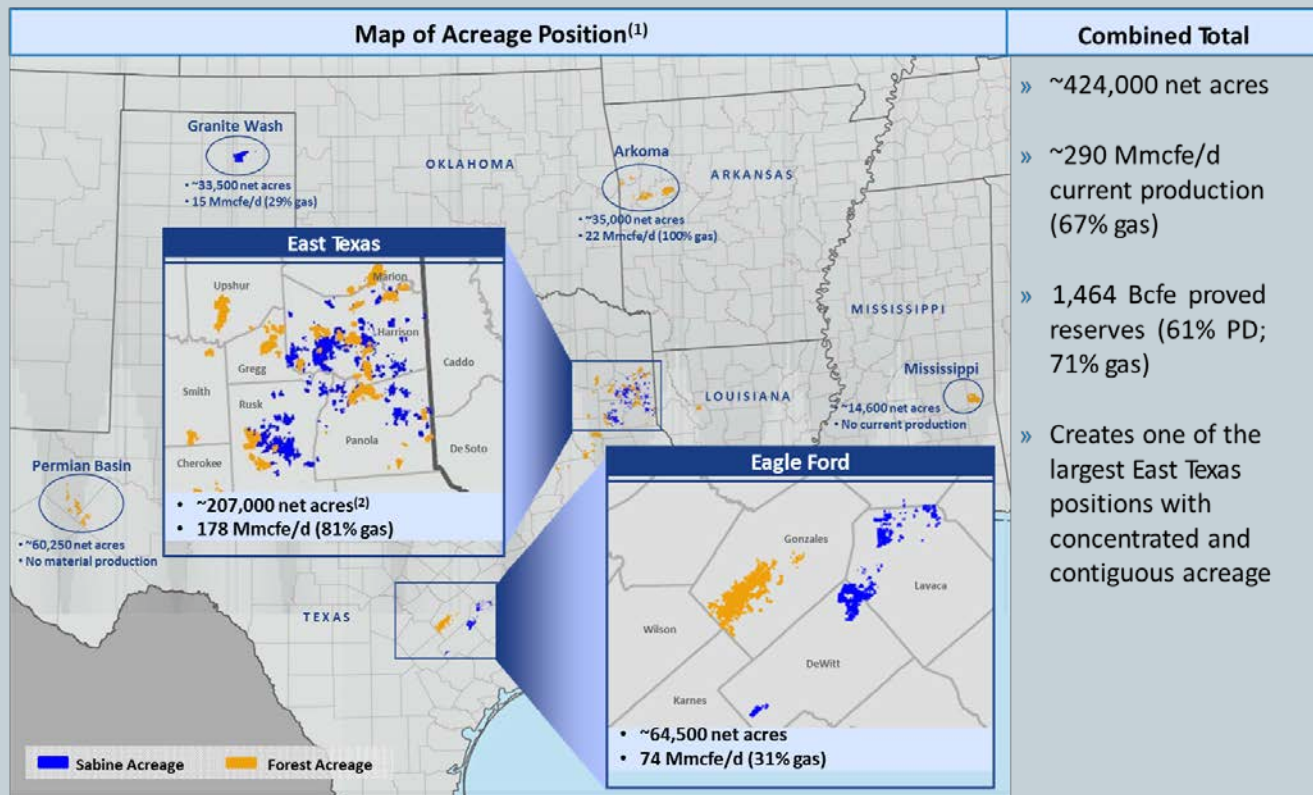


- Forest will reverse split 1:10, leaving roughly 12MM shares
- Sabine unit holders will be issued roughly 33MM shares
- Total Shares: 45MM @ \$23.00 = \$1.0B market cap
- Net debt (combined): 2.2B
- Current implied enterprise value: \$3.2B
- Expected close: Sep/Oct 2014
- Conditions:
  - Financing in place
  - Regulatory non-issue
  - Need 2/3 vote of FST shareholders

# Pro Forma Asset Profile



## Complementary Asset Footprints



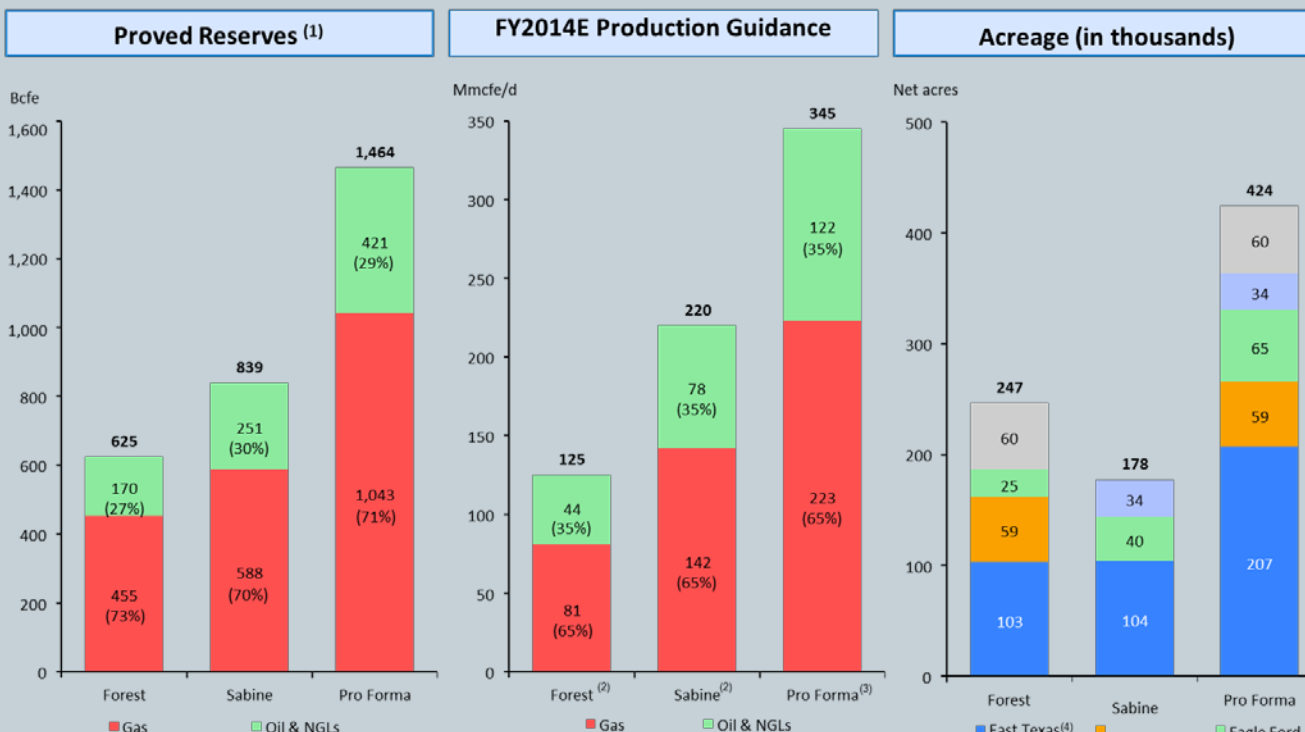
<sup>1</sup> Daily production representative of 1Q 2014 production  
<sup>2</sup> Does not include additional acreage in North Louisiana or ~71,000 DK exploratory net acres in East Texas

Source: Sabina Presentation 6/4/14

# Pro Forma Asset Profile



## Pro Forma Asset Profile



1 As of 12/31/13 Per  
 2 current guidance  
 3 Represents combination of current standalone guidance from Forest and Sabine management  
 4 Does not include additional ~71,000 DK net acres in East Texas  
 5 Excludes East Texas acreage

Source: Sabine Presentation 6/4/14

# Near-Term Catalysts



- Sabine has stated that they do not plan to issue equity in 2014 – 2015
- Leverage will decline from 4.6x to 3.3x through a combination of divestitures and production growth
- Existing debt will be refinanced over the next year in addition to debt issuances necessary to complete the merger
- Combined entity will be significantly more attractive to investors: \$23 stock, \$1.0B mkt cap, improving balance sheet and strong production growth
- Company should be actively covered by sell-side research
- First Reserve will likely sell shares (73.5%) through secondary offerings which will be promoted as increasing liquidity

# Long-Term Catalysts



- Divestitures will reduce leverage warranting re-rating of equity
- Starting in 2015, Company should shed 2/3 of Forest's SG&A expenses
- Optionality if Sabine's D&C performance and Forest's cost controls can improve returns on the combined asset portfolio, particularly legacy Forest

# What Is It Worth? - Net Asset Value



Private Market Analysis						
	<u>Pro Forma</u>	<u>Low</u>	<u>High</u>	<u>Low</u>	<u>High</u>	<u>Average</u>
Flowing production multiple (MMcfe/d, \$/MCfe/d)	290.0	\$4,000	\$ 6,000	\$ 1,160	\$ 1,740	\$ 1,450
Proved undeveloped reserves (BCfe,\$/MCfe)	998.1	2.00	3.00	1,996	2,994	\$ 2,495
Undeveloped Acreage (Ac, \$/Ac)	188,749	2,000	4,000	377	755	\$ 566
				\$ 3,534	\$ 5,489	\$ 4,511
Less: current net debt				\$ 2,177	\$ 2,177	\$ 2,177
Enterprise Value				\$ 1,357	\$ 3,312	\$ 2,334
NAV/Share				\$ 3.01	\$ 7.36	\$ 5.19
Upside				31%	220%	126%
EV/EBITDA				7.3x	11.4x	9.4x

Private Market Analysis						
	<u>Pro Forma</u>	<u>Low</u>	<u>High</u>	<u>Low</u>	<u>High</u>	<u>Average</u>
Flowing 2014E production multiple (MMcfe/d, \$/MCfe/d)	345.0	\$4,000	\$ 6,000	\$ 1,380	\$ 2,070	\$ 1,725
Proved undeveloped reserves (BCfe,\$/MCfe)	998.1	2.00	3.00	1,996	2,994	\$ 2,495
Undeveloped Acreage (Ac, \$/Ac)	188,749	2,000	4,000	377	755	\$ 566
				\$ 3,754	\$ 5,819	\$ 4,786
Less: current net debt				\$ 2,177	\$ 2,177	\$ 2,177
Enterprise Value				\$ 1,577	\$ 3,642	\$ 2,609
NAV/Share				\$ 3.50	\$ 8.09	\$ 5.80
Upside				52%	252%	152%
EV/EBITDA -(2014E PF EBITDA \$602MM)				6.2x	9.7x	8.0x

# What Is It Worth? - Comparables



	<u>Forest Oil (FST)</u>	<u>Sabine Oil &amp; Gas</u>	<u>Pro Forma</u>	<u>Comstock Resources (CRK)</u>	<u>Exco Resources (XCO)</u>	<u>Average Comps</u>	<u>Implied Price at Average Comps</u>		<u>Upside</u>
Cash (\$MM)	48	1	49	2	95				
Debt	800	1,355	2,226	949	1,500				
Net Debt	752	1,354	2,177	947	1,405				
Implied Market Cap	275	763	1,038	1,373	1,555				
Enterprise Value	1,027	2,117	3,215	2,321	2,960				
LTM EBITDA (\$MM)	169	313	482	315	409				
Proved Reserves (Bcfe)	625	839	1,464	585	1,124				
% Liquids	27%	30%	29%	23%	10%				
Proved Developed Reserves (Bcfe)	414	466	880	428	737				
PV-10	743	1,351	2,094	1,054	1,252				
Current Daily Production (Mmcfe/d)	105	185	290	184	366				
EV/LTM EBITDA	6.1x	6.8x	6.7x	7.4x	7.2x	7.3x	\$	2.98	29%
EV/Proved Reserves (\$/Mcf)	\$ 1.64	\$ 2.52	\$ 2.20	\$ 3.97	\$ 2.63	\$ 3.30	\$	5.90	156%
EV/Proved Developed Reserves (\$/Mcf)	\$ 2.48	\$ 4.54	\$ 3.65	\$ 5.42	\$ 4.01	\$ 4.72	\$	4.39	91%
EV/PV-10	\$ 1.38	\$ 1.57	\$ 1.54	\$ 2.20	\$ 2.36	\$ 2.28	\$	5.78	152%
EV/Daily Production (\$/Flowing Mcfe)	\$ 9,782	\$ 11,443	\$ 11,086	\$ 12,613	\$ 8,080	\$ 10,346	\$	1.83	-20%
Net Debt/LTM EBITDA	4.4x	4.3x	4.5x	3.0x	3.4x	3.2x			
Net Debt/PV-10	1.0x	1.0x	1.0x	0.9x	1.1x	1.0x			

# 2014E PF - Strong Growth at Sabine



## 2014 Financial Guidance



### Pro Forma Combined 2014E Guidance

	Low	-	High	Midpoint
<b>Production:</b>				
Natural Gas (Mmcf/d)	212	-	234	223
Oil (Bbl/d)	10,731	-	11,860	11,296
Natural Gas Liquids (Bbl/d)	8,552	-	9,452	9,002
<b>Total Production (Mmcfe/d)</b>	<b>328</b>	<b>-</b>	<b>362</b>	<b>345</b>
<b>Total Production (Mboe/d)</b>	<b>55</b>	<b>-</b>	<b>60</b>	<b>58</b>
<b>Operating Expenses:</b>				
Lease Operating / Workover Expense	\$0.75	-	\$0.85	\$0.80
Marketing, Transportation, Processing	\$0.25	-	\$0.35	\$0.30
Production & Ad Valorem Taxes <sup>(1)</sup>	\$0.35	-	\$0.40	\$0.38
General & Administrative Expense	\$0.39	-	\$0.44	\$0.42
<b>Total Operating Expense (\$ / Mcfe)</b>	<b>\$1.74</b>	<b>-</b>	<b>\$2.04</b>	<b>\$1.89</b>
<b>Capex:</b>				
Total Capex (\$ millions)	\$800	-	\$825	

<sup>1</sup> Production taxes assume price deck of \$3.50/Mcf gas and \$85/Bbl oil.



# What Is It Worth? - 2014 Forecast



<b>Production</b>	<b>Guidance Midpoint</b>	<b>Total Production (Bcfe/Mbbl)</b>	<b>Revenues (\$4/\$90)</b>	<b>Revenues (6/17/14 Strip)</b>
Natural Gas (Mmcfd)	223	81	\$ 326	\$ 379
Oil (Bbl/d)	11,296	4,123	371	410
Natural Gas Liquids (Bbl/d)	9,002	3,286	99	109
Total Production (Mmcfe/d)	345	125,925	\$ 795	\$ 899
<b>Expenses</b>			<b>Costs</b>	<b>Costs</b>
Lease Operating/Workover Expense	\$ 0.80		\$ 101	\$ 101
Marketing, Transportation, Processing	\$ 0.30		38	38
Production & Ad Valorem Taxes	\$ 0.38		48	48
General & Administrative Expense	\$ 0.42		53	53
Total Operating Expense (\$/Mcf)	\$ 1.90		\$ 239	\$ 239
EBITDA			\$ 556	\$ 660
EV/2014E PF EBITDA			5.8x	4.9x
Implied price @ 6.5x EV/2014E PF EBITDA (Includes \$400MM for int exp & Capex in excess of EBITDA)			\$ 4.08	\$ 5.58
Upside			77%	143%

# What Is It Worth? - 2015 Forecast



- Divestitures should shrink net debt
  - 218K net acres in Ark-La-Tex (59K), Eagle Ford (65K), North Texas (34K), Permian (60K)
  - If sold at \$5K/Acre as undeveloped land value (conservative), could yield \$1.1B gross
- Forest's Land is mostly held by production (HBP). Sabine's East Texas land is HBP but North Texas & Eagle Ford are not
  - If divestitures include North Texas & Eagle Ford, Capex sharply reduced by smaller footprint and removing need to drill to HBP
- 2/3 of Forest's G&A disappears (\$29MM savings off LTM G&A of \$43MM)
- Becomes a pure play on East Texas natural gas with a healthy balance sheet

# Risks



- Deal Closing
  - Financing rumors on 6/16/14 highlight investor skittishness
- Energy Prices
  - Sabine & Forest hedge some production
- Downside
  - Forest traded at \$1.79 prior to deal announcement: -22% downside

# Summary



- High conviction merger closes in 3-4 months
  - Downside to \$1.55 - \$1.75 -22% to -33% in unlikely event deal does not occur
- Market fails to recognize value for identifiable structural reasons
- Valuation creates large margin of safety
  - Most conservative estimate of value at \$3.00/share +30%
- Several near-term catalysts to close valuation gap with peers
  - Probable value 6 months out at \$4.00 - \$5.00/share +74% - +117%
- Long-term catalysts could result in substantial growth
  - Potential for additional value creation in 2015 beyond \$6.00/share +161%

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